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IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

No. 464

FIRST NATIONAL BANK IN HOUSTON, P. P. BUTLER, T. W. GREGORY, JR., LEON JAWORSKI, AND B. J. BRADSHAW,

Petitioners.

VS.

CHARLES M. LAKE, TRUSTEE OF PETROL TERMINAL CORPORATION AND SUBSIDIARY CORPORATIONS IN PROCEEDINGS FOR REORGANIZATION,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

HILARY W. GANS,
1904 First National Bank Building,
Baltimore 2, Maryland,

LEON JAWORSKI,
Second National Bank Bldg.,
Houston 2, Texas,

Counsel for Petitioners.

The Daily Record Co., Baltimore 3, Md.

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First National Bank in Houston, a national banking corporation, located and doing business in Houston, Texas, P. P. Butler, T. W. Gregory, Jr., Leon Jaworski, and B. J. Bradshaw pray that a writ of certiorari issue to review the judgment entered in this cause on October 7, 1952, by the United States Court of Appeals for the Fourth Circuit.

OPINIONS BELOW

There is a majority opinion (R. 96-109) and a dissenting opinion (R. 109-121). At the time of the filing of this Petition these opinions had not been reported.

JURISDICTION

A judgment of the Circuit Court of Appeals was entered on October 7, 1952 (R. 121). The jurisdiction of the Supreme Court is invoked under 11 U. S. C. A. 47c and 28 U. S. C. A. 1254(1).

QUESTIONS PRESENTED

I.

Whether Chapter X of the Bankruptcy Act denies the right of plenary trial to a claimant of an interest in property in his possession which is adversely claimed by the trustee in reorganization?

II.

Whether a court sitting in bankruptcy for the reorganization of a corporation may impose its summary processes upon a claimant of an interest in property in his possession without the appearance or consent of such claimant?

III.

Whether Chapter X of the Bankruptcy Act empowers a court sitting in bankruptcy for the reorganization of a corporation to enjoin the prosecution of an action against the trustee in the United States District Court in another jurisdiction for removal of cloud from title to property in the possession of the plaintiff, when the sole purpose of such action is to remove the adverse claim the trustee has made to such property?

STATEMENT

Petrol Terminal Corporation, hereinafter referred to as "Terminal" and its subsidiary, Petrol California Marketers, Inc., hereinafter referred to as "Marketers," became indebted to petitioner First National Bank in Houston in the amount of $1,100,000.00 on loans made between November 24, 1950, and January 12, 1951. This indebtedness was reduced by payments to approximately $839,000.00, as of February 8, 1951. Thereafter, as a result of payments aggregating $395,000.00 made between February 26, 1951 and April 12, 1951, the debt was further reduced to approximately $445,000.00, plus interest and attorneys' fees.

On April 17, 1951, Terminal and Marketers, to secure this balance, pledged to the petitioner bank certain shares of stock held by them in other corporations. The certificates of these shares were then delivered to the petitioner bank, together with stock powers.

On May 29, 1951, Marketers assigned to the petitioner bank, as additional collateral, all of its right, title, and interest under certain contracts with The California Oil Company.

The bank held physical possession in Texas of all of this collateral and of the monies paid on the debts at the time of the filing and approval of petition for adjudication of bankruptcy against Terminal in the District Court of the United States for the District of Maryland.

Thereafter, the proceedings against Terminal were converted to proceedings for reorganization under Chapter X of the Bankruptcy Act, and still later, petitions were filed for reorganization of Terminal's subsidiaries, including Marketers.

Charles M. Lake, having been appointed trustee for the debtor corporations in such proceedings, examined officers of the bank and other witnesses in regard to these transactions in a proceeding under Section 21(a) of the Bankruptcy Act. The examination was conducted in Houston, Texas pursuant to ancillary proceedings filed in the United States District Court for the Southern District of Texas. On February 13, 1952, the trustee filed a report with the court, fully relating the indebtedness to the petitioner bank, the payments and the security transactions recounted above, but stating, among other things, that in the opinion of the trustee the evidence developed through such examination indicated that the payments to the petitioner bank made between February 26, 1951 and April 12, 1951, and the transfers of the stocks and contracts to the bank constituted voidable preferences, recoverable by the trustee (R. 36-37). But no proceeding was instituted by the trustee for the recovery of the property transferred to petitioner bank.

On March 26, 1952, the bank filed a complaint in a civil action in the District Court of the United States for the Southern District of Texas, Houston Division, against Charles M. Lake as such trustee (R. 21-28). This suit was brought under 28 U. S. C. A. 1655 to remove the cloud cast by such claims of the trustee upon the right, title, and interest of the bank in the monies and properties claimed by the trustee and within the possession of the bank in the Southern District of Texas.

Such complaint seeks a determination by the District Court for the Southern District of Texas of the question whether the money payments and transfers of stock and contracts to the bank are voidable preferences, as claimed by the trustee. No judgment is sought against the trustee

or against the debtor corporations for the amount of the debt owing from the corporations to the bank. No foreclosure of lien or pledge upon the property in question is sought. By such suit the bank attempts to acquire no additional rights in any property of the debtor corporations; it seeks only to confirm the rights and interest transferred to it by the debtor corporations before the commencement of the proceedings for their reorganization. *As it relates to the trustee and the debtor corporations, it is in all respects exactly like a suit brought by the trustee for recovery of the money and property in the bank's possession on the ground that they were acquired by preferential transfers, except that the moving parties are reversed.* In its petition the bank pointed out the necessity of obtaining a removal of the cloud cast by the trustee, because of the probability that bank examiners, due to such cloud, would require the bank to charge off the collateral it held.

Without answering or pleading to said complaint, the trustee filed in the reorganization proceedings in Maryland a petition against the bank and its officers and attorneys (who join herein as petitioners) seeking, in addition to other relief, a permanent injunction against any further steps in the prosecution of the civil action pending in the Southern District of Texas without leave of the District Court in Maryland (R. 1-17).

Upon the filing of such petition, the District Court in Maryland on April 25, 1952, entered ex parte and without notice an order in the reorganization proceedings directing the bank and its officers and attorneys named herein as petitioners to appear and plead in answer to the petition of the trustee and enjoining them from proceeding further with the suit in the District Court for the Southern District of Texas (R. 17-20). Such order was served upon petitioners in the State of Texas.

Petitioners appeared specially in the reorganization proceedings and filed their motion to dissolve the injunction order of April 25, 1952, and to dismiss the trustee's petition against them on the ground that the court was without jurisdiction (R. 28-36). None of the petitioners has participated in the reorganization proceedings or otherwise submitted to the jurisdiction of the District Court of Maryland. Nor has petitioner bank filed a creditor's claim.

The court overruled petitioners' motion and continued the injunction in effect (R. 37-38).

Petitioners appealed from such order to the United States Court of Appeals for the Fourth Circuit, which rendered its opinion and judgment on October 7, 1952, in which the order of the District Court of Maryland was affirmed by the majority (R. 96-109). Mr. Justice Soper filed a dissenting opinion, upholding petitioners' contention (R. 109-121).

REASONS FOR GRANTING THE WRIT

I.

In the words of Mr. Justice Soper in his dissenting opinion, "The decision (in this case) necessarily involves the *important inquiry* as to the extent of the jurisdiction of the reorganization court to determine summarily adverse claims against the property of the bankrupt."

The majority opinion confers upon the court proceeding under Chapter X of the Bankruptcy Act a power repeatedly refused to other bankruptcy courts. It holds that in a proceeding under Chapter X of the Bankruptcy Act, the property rights of a party *in possession* under a claim adverse to a trustee may be subjected to the summary jurisdiction of the reorganization court without the claimant's consent. This Honorable Court in cases such as *Taubel-Scott-Kitzmiller Co. v. Fox*, 264 U. S. 426, 44 S. Ct. 396,

68 L. Ed. 770, has denied the Bankruptcy Court the right to exercise summary jurisdiction over property not in the possession or in the constructive possession of the court, without the consent of the party who was asserting an adverse claim to the trustee. In the instant case, the majority opinion holds that the valuable right to a plenary trial may be denied to claimants in possession holding adverse to the trustee where the proceeding is one under Chapter X of the Bankruptcy Act. In so holding, it is submitted that the majority opinion has interpreted erroneously a Federal statute.

On February 13, 1952, the trustee filed his report in the reorganization proceedings, asserting his belief that the property held by petitioner bank could be recovered. Such an adverse claim, when directed against assets of a bank, has serious consequences. The trustee took no action to pursue his claim; wherefore, petitioner bank on March 26, 1952 filed its action to remove the cloud cast by the trustee on the rights of the bank to the property in its possession. Thus, the bank put in issue in a plenary action the very question and issue the trustee would have had to litigate with the bank had the trustee taken the initiative. Moreover, it is submitted that had the trustee brought such an action, it would have had to have been in exactly the same forum selected by the bank, namely, the jurisdiction in which petitioner bank has its residence.

The majority opinion holds that the reorganization court has jurisdiction to enjoin the prosecution of the action filed by petitioner bank on the ground that such a suit invades a realm in which the jurisdiction of the reorganization court is *exclusive*. Obviously, if the reorganization court does not have jurisdiction to determine the subject matter

of the bank's suit without the consent of the bank, the holding of the majority is erroneous.

In reviewing the Congressional history of Chapter X of the Bankruptcy Act and the effect of the opinion in the case of *Bardes v. First National Bank,* 178 U. S. 524, 44 L. Ed. 1175, 20 S. Ct. 1000, this Honorable Court speaking through Chief Justice Vinson in the case of *Williams v. Austrian,* 331 U. S. 642, 91 L. Ed. 1718, 67 S. Ct. 1443, said:

> "Where §§60 (b), 67 (e), and 70 (e) were not involved, the Bardes rule continued to be applied where plenary proceedings were required, as in cases relating to property adversely held and suits upon choses in action belonging to the bankrupt's estate. Left for summary disposition under §2 were those proceedings in which the controversy related to property in the possession or constructive possession of the court or to property held by those asserting no truly adverse claim."

Not only in ordinary bankruptcy proceedings, but also in proceedings for reorganization of corporations has it been uniformly held that a trustee may not in a summary proceeding recover for the benefit of the debtor's estate on an obligation due to the debtor or recover property held in possession of an adverse claimant, without consent of the adverse party. *Warder v. Brady,* 115 Fed. (2d) 89 (4 Cir. 1940); *In re Mount Forest Fur Farms of America, Inc.,* 122 Fed. (2d) 232 (6 Cir. 1941, cert. den. 314 U. S. 701, 62 S. Ct. 480, 86 L. Ed. 561); *Duda v Sterling Manufacturing Co.,* 178 Fed. (2d) 428, 14 A. L. R. (2d) 899 (8 Cir. 1949); *Thompson v. Terminal Shares, Inc.,* 104 Fed. (2d) 1 (8 Cir. 1939).

The decision of the majority of the Court of Appeals is contrary to the law established by those cases. The major-

ity opinion attempts to distinguish those authorities on the ground that the interest claimed by the bank in the collateral in its possession is something less than absolute ownership.

This is made abundantly clear from the following quotations from the majority and dissenting opinions.

In the majority opinion (R. 108) it is stated:

> "Appellant fails to distinguish between the power of the reorganization court over property of the debtor which has been pledged as collateral security and which is held by the creditor merely as security for a debt and its power over property which is claimed adversely to the debtor by one who is in possession asserting absolute ownership. It is clear that the reorganization court may not exercise summary jurisdiction in the latter case but may exercise it in the former, and in the former case may protect its jurisdiction by proper use of its injunctive power * * *."

In the dissenting opinion Mr. Justice Soper said (R. 118):

> "This line of authority has led the court in the pending appeal to conclude that a reorganization court may not exercise summary jurisdiction over the property of the debtor in the possession of one who claims absolute title; and the court might have added, as the trustee concedes in his brief on this appeal, that a reorganization court also lacks summary jurisdiction over a suit by the trustee to recover a preferential payment to a creditor or to recover upon a claim due the bankrupt estate. We had previously come to these conclusions in *Warder v. Brady*, 4 Cir., 115 F. 2d 89, and Collier on Bankruptcy, Vol. 6, 584, is to the same effect. Hence it is obvious that Congress in its latest effort to establish a practicable and efficient scheme of reorganization still withholds from the reorganization court complete power over the property of the bankrupt and still protects adverse claimants to property of the

debtor in their possession from suits in a distant state. Accordingly it is frequently necessary for the trustee to engage in litigation outside the reorganization court before a plan of reorganization can be effectuated; and that will be necessary in the present proceeding unless the trustee abandons his claims for the return of the preferential payments alleged to have been made to the Bank.

"The area of disagreement is therefore restricted to the limited position that controversies over property of the bankrupt held by a creditor as collateral security for a debt of the bankrupt must be adjudicated in the bankruptcy court. This position cannot be defended on the ground that there is a substantial distinction in principle between a claim of a partial interest in property of the bankrupt and a claim of absolute title thereto. In each case the claim is adverse and the propriety of a suit against the claimant in the district of his residence is based on the same considerations."

The distinction made by the majority opinion is without support in a single reported case and cannot be defended on principle.

Had the Bank foreclosed its lien and purchased the collateral shortly prior to the filing of the petition for the reorganization of the debtor, the majority opinion would deny to the Bankruptcy Court jurisdiction to determine the validity of the Bank's claim to the collateral on the ground that the Bank would, in that case, be in possession and asserting absolute ownership, yet the majority opinion sustains the jurisdiction of the Bankruptcy Court because at the time of the filing of the reorganization petition the Bank had not foreclosed nor purchased the property but held possession, asserting only a security title. That the Bank does not claim absolute ownership of the collateral renders the interest it does claim none the less a right of

property; nor does it render such claim any less hostile and adverse to the trustee's claim of right to recover collateral free and clear of any and all claims and interest.

II.

The majority opinion of the Court of Appeals purports to follow a line of decisions illustrated by *Continental Illinois Bank & Trust Co. v. Chicago Rock Island and Pacific Railway Co.*, 294 U. S. 648, 55 S. Ct. 595, 79 L. Ed. 1110, and *Reconstruction Finance Corporation v. Kaplan*, 185 Fed. (2d) 791, in which it has been held that the jurisdiction of a reorganization court does extend to property in the possession of the debtor's creditors wherever located for *some* purposes, such as to enjoin threatened foreclosure. None of the decisions cited in the majority opinion support its decision, and actually, the majority opinion is in conflict with such cases, in principle. In all of the cases on which it relies, the party in possession *was recognized as a secured creditor*, and his right to his security was *not* disputed, but was protected. In *Reconstruction Finance Corporation v. Kaplan*, supra, on which the majority opinion relies, it was held at page 796:

> "While a court, pending working out of a reorganization, may interfere with and postpone the secured creditor's remedy, it must be careful not to impair his substantive rights."

The quoted ruling of the Court of Appeals for the First Circuit follows the decision of this Honorable Court in *Continental Illinois Bank & Trust Co. v. Chicago Rock Island and Pacific Railway Co.*, supra. In that case this Court said at page 680:

> "It is next contended that the court was without power to issue the injunction in a summary proceeding. Obviously, an application for an injunction against the

immediate enforcement of a remedy is not the assertion of an adverse claim. The bonds deposited as collateral were not in the hands of purchasers, but in the hands of creditors as security. That the equity which the debtor retained was a property interest was not and could not be disputed by the creditors; nor was the claim of the creditors in respect of their rights in the collateral security or the rank of their liens questioned by the debtor. In short, no adverse claim was brought forward by either of the parties to the controversy. The only question was in respect of the creditors' remedy; and the sole point is as to the authority of the bankruptcy court to delay for a reasonable time an interference with the reorganization proceeding which would result from an immediate sale of the collateral."

III.

The suit filed by Petitioner Bank against the trustee is a plenary suit in which the trustee is afforded the opportunity to recover property which he claims for the benefit of the debtors. If such suit had been filed by the trustee, under the express decision of this Honorable Court in *Williams v. Austrian,* supra, the District Court for the Southern District of Texas would have had jurisdiction to try the cause. Yet, the Court of Appeals holds that such suit, when filed by the Bank, is an invasion of the *exclusive* jurisdiction of the reorganization court. It is inconceivable that the doors of a court should be open to one party to a controversy, yet be closed to the other party on the ground that the court lacks jurisdiction of the subject matter of the controversy.

CONCLUSION

The decision of the court below involves an important question of Federal law which has not been, but should be, settled by this Court.

The decision is in conflict with the overwhelming weight of authority prior to and following the enactment of Chapter X of the Bankruptcy Act and with the principles of the applicable decisions of this Court herein referred to.

The decision is one of great public importance as it does violence to the general policy of Congress that persons should not be subjected to civil suits except in the district of which they are inhabitants.

Respectfully submitted,

HILARY W. GANS,

LEON JAWORSKI,

Counsel for Petitioners.